Supreme Court, U.S.
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No. 01-

IN THE

# Supreme Court of the United States

ROBERT J. MATZ, Individually and on Behalf of All Others Similarly Situated,

*Petitioner,*

*v.*

HOUSEHOLD INTERNATIONAL TAX REDUCTION INVESTMENT PLAN,

*Respondent.*

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

## PETITION FOR A WRIT OF CERTIORARI

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## QUESTIONS PRESENTED FOR REVIEW

1. Whether all terminated plan participants in a qualified employee benefit plan, regardless of vesting status at the time of termination, should be counted to determine whether a partial termination of the plan has occurred.

2. When a regulation is ambiguous or silent as to the question at issue, yet gives the responsible agency broad interpretive powers, and the agency has issued an interpretation of the regulation, whether a court may refuse to consider the agency's interpretation of the regulation, thus abandoning the regulatory deference standards set forth in *Auer v. Robbins*, 519 U.S. 452, 117 S. Ct. 905 (1997).

3. When both the applicable statute and regulation are silent or ambiguous as to the question at issue and the responsible agency has issued informal interpretations of both the statute and the regulation, should a court apply the standards of judicial deference of both *United States v. Mead Corp.*, 121 S. Ct. 2164 (2001), and *Auer v. Robbins*, 519 U.S. 452, 117 S. Ct. 905 (1997), to the agency's interpretations.[1]

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1. If this Court meant for the statutory interpretation standards set forth in *Mead* to apply to an agency's interpretation of its own regulations, then Petitioner respectfully requests that this Petition be granted and that this case be remanded to the Seventh Circuit for its reconsideration of the regulation at issue here. In the event this Court determines *Mead*, and not *Auer*, applies to an agency's interpretation of its own regulation, then Petitioner submits that the IRS' interpretation of the partial termination regulation clearly meets the *Mead* standards because the regulation expressly gives the IRS the authority to decide what facts and circumstances are relevant to the partial termination determination. Reg. § 1.411(d)-2(b)(1).

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Matz petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Seventh Circuit.

## OPINIONS BELOW

The opinion of the Seventh Circuit, on remand, which is reported at 265 F.3d 572, is reproduced at Appendix ("App.") 1a-7a. This Court's order granting Respondent's Petition for Writ of Certiorari and vacating the Seventh Circuit's initial opinion, which is reported at 121 S. Ct. 2545, is reproduced at App. 8a. The initial opinion of the Seventh Circuit, which is reported at 22 F.3d 971, is reproduced at App. 9a-21a. The November 30, 1998 opinion and order of the district court appears at 1998 WL 851491 and is reproduced at App. 22a-33a.

The Seventh Circuit's order of October 16, 2001, denying Petitioner's Petition for Rehearing with Suggestion for Rehearing *En Banc* of the second opinion is reproduced at App. 34a-35a.

## STATEMENT OF JURISDICTION

Petitioner invokes this Court's jurisdiction pursuant to 28 U.S.C. § 1254(1). The Seventh Circuit filed its order denying rehearing on October 16, 2001. App. 34a. This Petition is filed within ninety days of that date.

## STATUTES AND REGULATIONS

28 U.S.C. § 1331:

> The district courts shall have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States.

Internal Revenue Code ("IRC") § 401(a)(7), 26 U.S.C. § 401(a)(7):

> A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part satisfies the requirements of section 411 (relating to minimum vesting standards).

IRC § 411(d)(3)(A), 26 U.S.C. § 411(d)(3)(A):

> **Termination or partial termination; discontinuance of contributions.** Notwithstanding the provisions of subsection (a), a trust shall not constitute a qualified trust under section 401(a) unless the plan of which such trust is a part provides that —
>
> > (A) upon its termination or partial termination . . .
>
> the rights of all affected employees to benefits accrued to the date of such termination, partial termination, or discontinuance, to the extent funded as of such date, or the amounts credited to the employees' accounts, are nonforfeitable. This paragraph shall not apply to benefits or contributions which, under provisions of the plan adopted pursuant to regulations prescribed by the Secretary to preclude the discrimination prohibited by section 401(a)(4), may not be used for designated employees in the event of early termination of the plan.

Employee Retirement Income Security Act ("ERISA") § 3(34), 29 U.S.C. § 1002(34):

> The term "individual account plan" or "defined contribution plan" means a pension plan which provides for an individual account for each participant and for benefits based solely upon the amount contributed to the participant's account, and any income, expenses, gains and losses, any forfeitures of accounts of other participants which may be allocated to such participant's account.

ERISA § 501(a)(1)(B), 29 U.S.C. § 1132(a)(1)(B):

> **(a) Persons empowered to bring a civil action**
>
> A civil action may be brought —
>
> (1) by a participant or beneficiary —
>
> (B) to recover benefits due him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan.

ERISA § 501(e)(1), 29 U.S.C. § 1132(e)(1):

> Except for actions under subsection (a)(1)(B) of this section, the district courts of the United States shall have exclusive jurisdiction of civil actions under this title brought by the Secretary or by a participant, beneficiary, fiduciary or any person referred to in section 101(f)(1). State courts of competent jurisdiction and district courts of the United States shall have concurrent jurisdiction of actions under paragraphs (1)(B) of (7) of subsection (a) of this section.

ERISA § 501(f), 29 U.S.C. § 1132(f):

> The district courts of the United States shall have jurisdiction, without respect to the amount in controversy or the citizenship of the parties, to grant relief provided for in subsection (a) of this section in any action.

Treasury Regulation § 1.401-6(b), 26 C.F.R. § 1.401-6(b):

> *Termination defined.* (1) Whether a plan is terminated is generally a question to be determined with regard to all the facts and circumstances in a particular case . . .
>
> > (2) For purposes of this section, the term termination includes both a partial termination and a complete termination of a plan. Whether or not a partial termination of a qualified plan occurs when a group of employees who have been previously covered by the plan are subsequently excluded from such coverage either by reason of an amendment to the plan, or by reason of being discharged by the employer, will be determined on the basis of all the facts and circumstances . . . [I]f a partial termination of a qualified plan occurs, the provisions of section 401(a)(7) and this section apply only to the part of the plan that is terminated.

Treasury Regulation § 1.411(d)-2(b)(1), 26 C.F.R. § 1.411(d)-2(b)(1):

> Whether or not a partial termination of a qualified plan occurs (and the time of such event) shall be determined by the Commissioner with regard to all the facts and circumstances in a particular case. Such facts and circumstances include: the exclusion, by reason of plan amendment or severance by the employer, of a group of employees who have been previously covered by the plan . . . .

## STATEMENT OF THE CASE

### A. Introduction.

Petitioner asks this Court to resolve the direct conflict between the Circuit Courts concerning an important issue that arises when courts are asked to determine whether a qualified employee benefit plan has been "partially terminated," thus requiring full vesting of the benefits of all affected employees. More importantly, while *United States v. Mead*, 121 S. Ct. 2164 (2001), left intact this Court's rule, most recently set forth in *Auer v. Robbins*, 519 U.S. 452, 117 S. Ct. 905 (1997), that an agency's interpretation of its own ambiguous or silent regulation is to be given substantial judicial deference by the courts, the Seventh Circuit applied *Mead* so as to abrogate this rule. The Seventh Circuit's decision effectively rejects *Auer* and its principles, and permits courts to set aside an agency's reasonable interpretation of its own regulation, thus allowing litigants and the courts to advance their own interpretation of the agency's regulation.

### B. Background Facts.

Petitioner, Robert J. Matz, and other employees of Hamilton Investments, Inc. ("Hamilton"), a subsidiary of Household

International, Inc. ("Household"), lost their jobs and the non-vested portions of their pension plan in September of 1994, when the assets of Hamilton were sold. Household sponsors Respondent, a defined contribution employee pension plan, for both Household's employees and the employees of its subsidiaries, such as Hamilton. Subsequent to the sale of Hamilton's assets, Household, pursuant to a plan of reorganization, proceeded with the sale of several other businesses and the termination of related employees and participants in Respondent.

Respondent is intended to be a qualified profit sharing plan under IRC § 401(a). Household makes matching contributions to Respondent on behalf of those employees who have chosen to participate in Respondent with their own contributions. All contributions by participants to Respondent are completely vested, regardless of the length of time such participants have been employed with Household. However, until September 1995, Household's matching contributions to Respondent on behalf of each participant were vested over a five-year period. During that five-year period, a participant would vest in the matching contributions at the rate of 20% per year. Accordingly, a participant in Respondent would be fully vested after five years of participation. If five years of participation was not achieved by a participant, the unvested portion of Household's matching contributions was forfeited to Respondent and would reduce Household's future contributions to Respondent.

In September 1995, during the period of time that Household was selling off other businesses and terminating a substantial number of employees, Respondent was amended to eliminate the five-year vesting schedule. As a result, all remaining participants in Respondent were fully vested in their respective accounts, including Household's matching contributions to their accounts.

Petitioner participated in Respondent until the time of his termination on September 1, 1994, when Household sold Hamilton's assets. At the time of his termination, Petitioner was 60% vested in the matching contributions made by Household and credited to his account. Petitioner was given $27,914.10, the full amount of his vested account. The remaining unvested portion of Household's matching contributions, $7,289.92, was forfeited back to Respondent.

**C. Petitioner's Lawsuit.**

Petitioner filed the underlying class action in the United States District Court for the Northern District of Illinois in February 1996, on behalf of himself, and all of those persons similarly situated, pursuant to ERISA §§ 502(a)(1)(B), 29 U.S.C. § 1132(a)(1)(B). The district court has subject matter jurisdiction pursuant to 28 U.S.C. § 1331 and ERISA §§ 502(e)(1) and (f), 29 U.S.C. §§ 1132(e)(1) and (f), without respect to the amount in controversy or the citizenship of the parties.

Petitioner asserted that Household sold Hamilton as part of a stated, overall plan to refocus its business. That business plan also included the sale of Household's residential mortgage business, its mortgage servicing business, its banking business and a life insurance subsidiary. Petitioner alleged that, as a result, a partial termination of Respondent had occurred and, therefore, Petitioner was entitled to the full amount of his pension account.[2]

2. Courts have generally held a "partial termination" of a qualified employee benefit plan only occurs where there has been a significant reduction in plan participants. In determining whether there has been a significant reduction, courts apply the "significant percentage" test. *Kries v. Charles O. Townley, M.D. & Associates, P.C.*, 833 F.2d 74, 79 (6th Cir. 1987). In applying such a test, courts look to see whether a significant percentage of plan participants have been terminated. If so, then the plan is deemed to have been partially terminated and all involuntarily terminated participants become entitled to full vesting of their benefits. *Kries*, 833 F.2d at 79-80.

Petitioner's allegation was based on the specific provision within the documents creating Respondent that states:

> in the case of the termination of [Respondent] by Household International, Inc. . . . or a partial termination of [Respondent] with respect to a group of participants, the account balance of each affected participant shall become 100% vested.

**D. The District Court's Rulings In Favor Of Petitioner.**

In December 1997, Respondent moved for partial summary judgment to exclude those participants who were terminated after September 1995, when Respondent was amended, from both any partial termination analysis and from the plaintiff class itself. In denying Respondent's motion, the district court held that fully vested plan participants are counted in the partial termination analysis, but that such participants are excluded from the plaintiff class. App. 33a.

Respondent moved again for partial summary judgment on December 31, 1998, on the issue of whether events occurring in multiple plan years can be considered in determining if a partial termination has occurred. The district court denied that motion on September 8, 1999, and held that terminations occurring over multiple plan years may be aggregated for the purpose of the partial termination analysis. App. 21a.

**E. Respondent's Interlocutory Appeal To The Seventh Circuit.**

On November 30, 1999, the district court granted Respondent's motion to certify the November 30, 1998 and September 8, 1999 orders for interlocutory appeal. The specific questions certified for review by the Seventh Circuit were: (i) whether, for purposes of determining if a partial termination

of Respondent had occurred, fully-vested plan participants should be included in the partial termination analysis, and (ii) whether the partial termination analysis may include terminations that take place over multiple plan years. App. 13a. The Seventh Circuit granted Respondent's request for a permissive, interlocutory appeal of these issues on January 3, 2000. App. 10a.

### F. The Seventh Circuit's Initial Opinion In Favor Of Petitioner.[3]

The Seventh Circuit issued an opinion ("First Opinion") affirming both orders of the district court. App. 21a. In the First Opinion, the Seventh Circuit reviewed the partial termination statute and its legislative history as well as the corresponding Treasury Regulation and concluded that both the statute and the regulation were ambiguous as to the standard for determining when a partial termination has occurred. In doing so, the Seventh Circuit specifically noted that "[n]either the statute, its legislative history nor the Treasury Regulation . . . differentiate between vested and non-vested participants." App. 18a.

Because of this silence, the Seventh Circuit next looked to the Second Circuit's description of, and deference to, the Internal Revenue Service's ("IRS") position with respect to the interpretation of both the partial termination statute *and* the partial termination regulation, as set forth in an *amicus curiae* brief submitted by the IRS to the Second Circuit upon that Court's request in *Weil v. Retirement Plan Administrative*

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3. In its First Opinion, the Seventh Circuit also affirmed the district court's ruling that involuntary terminations occurring over multiple plan years may be aggregated for the purpose of determining whether a partial termination has occurred. App. 21a. Because *Mead* did not impact this ruling, the Seventh Circuit reaffirmed this ruling in its Second Opinion. App. 6a-7a.

*Committee of the Terson Co., Inc.*, 933 F.2d 106 (2d Cir. 1991) ("*Weil III*"),[4] and as also set forth in the Internal Revenue Manual ("*Manual*"), Subsection 7753 § 252(7) (1990). A copy of the IRS' *amicus curiae* brief is reproduced at App. 36a-52a. The IRS has interpreted both the partial termination statute *and* regulation to require that all participants — including those fully vested — be counted for purposes of a partial termination analysis. App. 46a; *Manual*, Subsection 7753 § 252(7) (1990). In the brief, the IRS discusses at length the all inclusive language of both the partial termination statute and the regulation, the IRS' interpretation of the statute and regulation, the analysis and rationale underlying the interpretation, the statute's legislative history and purpose, relevant case law and IRS rulings, opinions and publications supporting the interpretation. App. 43a-50a.

Because the IRS had issued its interpretation of both the partial termination statute and regulation, the Seventh Circuit, in its First Opinion, limited its analysis to whether the IRS' interpretation was reasonable. App. 18a. The Seventh Circuit cited to the *Weil III* Court's finding that the IRS' interpretation was reasonable, stated that the partial termination regulation *supports* such a finding by virtue of its all inclusive language, and held that the IRS' interpretive rule was reasonable, and therefore, fully vested plan participants are to be included in the partial termination analysis.[5] App. 18a-19a. On November

4. The IRS was not a litigant in *Weil III*. Rather, the Second Circuit specifically requested that the IRS submit an *amicus curiae* brief to provide the Court with the IRS' interpretation, and analysis and reasoning of that interpretation, of the partial termination statute and partial termination regulation. *Weil III*, 933 F.2d at 107.

5. The *Weil III* Court deferred to the IRS' interpretation of the partial termination statute pursuant to *Chevron U.S.A., Inc. v. Natural*

(Cont'd)

6, 2000, the Seventh Circuit denied Respondent's petition for rehearing with suggestion for rehearing *en banc*.

**G. Respondent's Petition For A Writ Of Certiorari.**

After the Seventh Circuit denied Respondent's petition for rehearing with suggestion for rehearing *en banc*, Respondent filed a Petition for a Writ of Certiorari with this Court, which Petition was granted without opinion. App. 8a. In its order, this Court vacated the First Opinion and remanded the case for further consideration in light of *United States v. Mead Corp.*, 121 S. Ct. 2164 (2001). App. 8a.

**H. The Seventh Circuit's Second Decision.**

On remand from this Court, the issue before the Seventh Circuit was whether this Court's analysis in *Mead* for determining the deference to be accorded an agency's informal statutory interpretation either (i) made the Seventh Circuit's deference to the IRS' interpretation of the partial termination statute inappropriate or misplaced, or (ii) changed the standards for determining whether deference to an agency's interpretation of its ambiguous regulation is warranted.

In its Second Opinion, the Seventh Circuit stated that it had given *Chevron* deference to the IRS interpretation of the partial termination statute and regulation under the stricter pre-*Mead* standards.[6] App. 3a. Despite apparently giving *Chevron*

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*Res. Def. Council, Inc.*, 467 U.S. 837, 104 S. Ct. 2778 (1984). *Weil III*, 933 F.2d at 108, 110. In its First Opinion, the Seventh Circuit apparently agreed with the *Weil III* Court's decision to so defer to the IRS' interpretation. App. 3a-4a.

6. Petitioner submits that if the Seventh Circuit gave *Chevron* deference to the IRS' interpretation of the partial termination statute

(Cont'd)

deference to the IRS' interpretation of the partial termination statute under the stricter pre-*Mead* standards, the Seventh Circuit found that the IRS' interpretation of the partial termination statute was an informal agency pronouncement not entitled to *Chevron* deference, but was instead afforded only deference under *Skidmore v. Swift & Co.*, 323 U.S. 134, 65 S. Ct. 161 (1944), based upon the interpretation's thoroughness, validity, consistency and persuasiveness. App. 5a. Thus, it appears that the Seventh Circuit has read *Mead* in such a manner as to restrict *Chevron* deference, as opposed to liberalizing it, which appears to be at odds with the intent of the *Mead* Court.

The Seventh Circuit then opined that the IRS' position on the partial termination statute, which the Court had previously found to be reasonable under *Chevron*, is unpersuasive. App. 6a. The Seventh Circuit held that "since we indicated [in the First Opinion] that if we were writing on a blank slate we would have held differently, we now adopt a rule that only non-vested participants should be counted in determining whether partial termination of a pension plan has occurred." App. 6a. In so ruling, the Seventh Circuit rejected the positions advocated by the Petitioner, Respondent and the IRS,[7] and instead adopted a

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(Cont'd)

under the stricter judicial deference standards in place at the time of the First Opinion, then in the post-*Mead* Second Opinion, *Chevron* deference should have also been given to the IRS' interpretation. At a minium, the Seventh Circuit should have deferred to the IRS' interpretation of the partial termination regulation as required by this Court in *Auer*. (*See* II, *infra*, at 17-26.)

7. Respondent takes the position that involuntarily terminated fully vested plan participants should be excluded from in the numerator, but included in the denominator, of the partial termination analysis. Petitioner and the IRS take the position that such participants should be included

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position supported only by *In re Gulf Pension Litigation*, 764 F. Supp. 1149 (S.D. Tex. 1991), a district court case issued prior to the publication of the IRS' position in *Weil III*.

Furthermore, in the Second Opinion, the Seventh Circuit failed to address or even mention that the IRS has also interpreted the partial termination regulation, which regulation the Seventh Circuit stated was silent as to whether fully vested participants are included in the partial termination analysis. App. 6a, 18a. The Seventh Circuit gave no deference to the IRS' interpretation of the ambiguous partial termination regulation, which deference is mandated by this Court's holding in *Auer v. Robbins*, 519 U.S. 452, 117 S. Ct. 905 (1997): if a regulation is ambiguous, a court must defer to an otherwise non-binding agency interpretation of that regulation unless the interpretation is plainly erroneous or inconsistent with the regulation.

In failing to apply the judicial deference standards set forth in *Auer* to the IRS' interpretation of its own ambiguous regulation, and instead only applying the standards of *Mead*, the Seventh Circuit misreads *Mead* as implicitly overruling *Auer*. Further, this failure to defer to the IRS' interpretation of the partial termination regulation also ignores the express terms of the regulation which provides that "[w]hether or not a partial termination of a qualified plan occurs . . . *shall be determined by the Commissioner*. . . ." Reg. § 1.411(d)-2(b)(1) (emphasis added).

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(Cont'd)
in both the numerator and the denominator. The Seventh Circuit took neither of these positions, but instead fashioned it's own position that fully vested plan participants are excluded from both the numerator and the denominator. App. 7a.

On September 21, 2001, Petitioner filed a Petition for Rehearing With Suggestion for Rehearing *En Banc*, which the Seventh Circuit denied on October 16, 2001. App. 34a.

## REASONS FOR GRANTING THE WRIT

### I. THE SEVENTH CIRCUIT'S DECISION THAT FULLY VESTED PLAN PARTICIPANTS ARE NOT INCLUDED IN THE PARTIAL TERMINATION ANALYSIS DIRECTLY CONFLICTS WITH A SECOND CIRCUIT DECISION WHICH HOLDS THE OPPOSITE.

The issue is whether fully vested plan participants who have been involuntarily terminated from plan participation are to be counted to determine if a qualified plan has been partially terminated. The IRS' long-standing rule, which has been consistently applied by the IRS since 1990, is that all plan participants, regardless of vesting status, are counted to determine whether a partial termination has occurred. *Weil III*, 933 F.2d at 110; *Manual*, Subsection 7753 § 252(7) (1990). Generally, where there is a 20% or more reduction in plan participation, a partial termination of the plan will be deemed to have occurred, and the affected employees (*i.e.*, the non-vested participants) are entitled to full vesting of their account balances. *Halliburton Co. v. Comr.*, 100 T.C. 216, 237 (1993). Thus, the important issue of which participants are to be counted in the partial termination could profoundly influence whether the plan experienced a reduction of 20% or more in participation and whether those affected participants receive full vesting of their account balances as required by law. IRC § 411(d)(3)(A).

In its Second Opinion, the Seventh Circuit decided that "only non-vested participants should be counted in determining whether partial termination of a pension plan has occurred" and

expressly rejected the IRS' long-standing and consistently applied interpretation of both the partial termination statute and partial termination regulation (*i.e.*, all plan participants, regardless of vesting status, are counted in the partial termination analysis). App. 6a. Now, within the geographical area covered by the Seventh Circuit, a qualified plan is allowed to disregard involuntarily terminated fully vested plan participants when determining whether it has been partially terminated.

The Second Circuit has reached the direct opposite conclusion. In *Weil III*, the Second Circuit held that fully vested plan participants who were involuntarily terminated from future participation *should* be counted in determining whether partial termination of a pension plan has occurred. *Weil III*, 933 F.2d at 110-11. In reaching this decision, the Second Circuit expressly relied upon and deferred to the IRS' interpretation in an *amicus curiae* brief submitted by the IRS to the Second Circuit.[8] Thus, within the geographical area covered by the Second Circuit, a qualified plan is *not* allowed to disregard involuntarily terminated fully vested plan participants when determining whether it has been partially terminated.

Obviously, there is now a direct conflict between the Seventh and Second Circuits regarding the appropriate test to be used to determine whether a qualified plan has been partially terminated. Significantly, there is now a direct conflict between the Seventh Circuit and the IRS, the agency responsible for enforcing the partial termination statute and regulation, and the agency which has express authority under the partial termination regulation to determine what facts and circumstances are relevant to the partial termination analysis. Reg. § 1.411(d)-2(b)(1). The purpose of federal law is to establish uniform federal standards. *Fort Halifax Packing Co. v. Coyne*, 482 U.S. 1, 9,

8. The *Weil III* Court deferred to the IRS' interpretation under the stricter pre-*Mead* standards. Presumably, the *Weil III* Court would also defer to the IRS' interpretation under the more relaxed *Mead* standards.

107 S. Ct. 221 (1987). Because ERISA governs *all* qualified employee benefit plans, regardless of where the employer or participants are located, uniformity is particularly important with respect to issues arising under ERISA because of its nationwide impact. *Patterson v. Shumate*, 504 U.S. 753, 765, 112 S. Ct. 2242 (1992). In fact, Congress intended for the federal courts to develop a federal common law for ERISA matters. *Shaw v. Delta Airlines*, 463 U.S. 85, 105, 103 S. Ct. 2890 (1983).

Because of the conflicting rulings on whether fully vested plan participants are included in the partial termination analysis, qualified plans with participants in the geographical areas covered by *both* the Seventh and Second Circuits face the ultimate dilemma – which partial termination standard to apply. Even if a qualified plan only has participants in the Seventh Circuit, the problem still remains because the plan faces a different standard being applied by the IRS. Furthermore, this conflict between Circuits and the IRS encourages participants to "forum shop."

For example, does the qualified plan make two partial termination analyses, one for the participants covered by the Seventh Circuit and one for the participants covered by the Second Circuit, thus subjecting itself to possible discrimination claims? Or does the qualified plan make only one partial termination analysis, thus subjecting itself to possible claims for benefits from the participants in another Circuit applying that Circuit's law? Does a qualified plan which excludes fully vested participants from the analysis and finds that no partial termination has occurred open itself up to a claim by the IRS that, in fact, a partial termination has occurred because the IRS includes fully vested participants? Does a qualified plan then face the loss of its qualified status?

Employers and qualified plans alike will continue to be faced with conflicting directives with serious consequences. Petitioner respectfully submits that these are questions which should be addressed by uniform standards in the federal courts, not by employers on a case-by-case basis. Thus, review by this Court of the Second Opinion is necessary, and this Petition should be granted.

## II. THE SEVENTH CIRCUIT'S DECISION TO GIVE NO DEFERENCE TO THE IRS' INTERPRETATION OF ITS AMBIGUOUS REGULATION DIRECTLY CONFLICTS WITH SUPREME COURT LAW AND LAW OF OTHER CIRCUIT COURTS.

### A. In Applying Mead To The IRS' Interpretation Of The Partial Termination Regulation, The Seventh Circuit Has Abandoned *Auer*.

In its Second Opinion, the Seventh Circuit focused solely on the statutory aspect of this case under *Mead* and failed to consider or even address the regulatory aspect of this case. The regulatory aspect of this case is governed by *Auer*, which provides that an agency's interpretation of an ambiguous or silent regulation is entitled to significant judicial deference. *Auer*, 519 U.S. at 461, 117 S. Ct. 905. Despite this controlling law, the Seventh Circuit failed to analyze the IRS' interpretation of the partial termination *regulation* under the judicial deference standards set forth in *Auer*, apparently abandoning this case.[9]

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9. The *Mead* Court did not overrule *Auer* or otherwise indicate it was no longer good law. "It is the Supreme Court's prerogative alone to overrule one of its precedents." *State Oil Co. v. Khan*, 522 U.S. 3, 20, 118 S. Ct. 275 (1997). "An intermediate appellate court has no authority to abandon governing case law from the Supreme Court." *Gordon v. United Airlines, Inc.*, 246 F.3d 878, 885 (7th Cir. 2001).

Instead, the Seventh Circuit focused solely on whether the IRS' interpretation was entitled to either *Chevron* or *Skidmore* deference. Although the Seventh Circuit had, in the First Opinion, afforded the IRS' interpretation *Chevron* deference under the stricter pre-*Mead* standards of the Seventh Circuit, in its Second Opinion, the Seventh Circuit found that the IRS' interpretation of the partial termination statute was not formal enough to warrant the deference described in *Chevron*. App. 4a-5a. Petitioner respectfully submits that this failure to give *Chevron* deference under the less stringent standards set by *Mead* is at odds with the purpose of *Mead*: to allow *Chevron* deference to be given to a broader range of agency actions and decisions.

In the Second Opinion, after concluding that *Chevron* did not apply, the Seventh Circuit held that, pursuant to *Skidmore*, the IRS' interpretation was entitled to "respect only to the extent those interpretations have the power to persuade." App. 5a. Despite the fact that the partial termination regulation *expressly* gives the IRS the power to determine what facts and circumstances are relevant in determining whether a partial termination of the plan has occurred, Reg. § 1.411(d)-2(b)(1), the Seventh Circuit found itself to be unpersuaded by the IRS' interpretation. Thus, in its Second Opinion, the Seventh Circuit gave the IRS' interpretation absolutely no deference. App. 6a.

The Seventh Circuit should not, however, have stopped its analysis at *Skidmore*. In doing so, the Seventh Circuit failed to take one additional and necessary step and consider the IRS' interpretation of the ambiguous partial termination ***regulation*** (as opposed to the partial termination statute), which interpretation is set forth in both the Manual and the *amicus curiae* brief submitted by the IRS to the Second Circuit in *Weil III*. The IRS has interpreted the partial

termination regulation to require the inclusion of all plan participants, regardless of vesting status, in the partial termination analysis. App. 44a-46a; *Manual*, Subsection 7753 § 252(7) (1990). Clearly, this determination is within the broad authority given to the IRS by the partial termination regulation. Reg. § 1.411(d)-2(b)(1).

The Seventh Circuit did not, however, analyze the IRS interpretation in light of the silent partial termination regulation, but instead treated the statutory and regulatory aspects as one and the same and *only* analyzed the IRS' interpretations in light of *Mead*, *Chevron* and *Skidmore*. Those decisions, however, apply only to an agency's interpretation, whether formal or informal, of an ambiguous statute; they do not apply to an agency's interpretation of its own ambiguous regulation. *Mead*, 121 S. Ct. at 2171, 2181; *Chevron*, 476 U.S. at 842-43, 104 S. Ct. 2778; *Skidmore*, 323 U.S. at 140, 65 S. Ct. 161. Indeed, it is clear that the Seventh Circuit treated statutory deference and regulatory deference interchangeably. For example, in its analysis of case law, the Seventh Circuit fails to distinguish between statutory and regulatory interpretations, and between deference give under *Chevron* and deference given under *Auer*. App. 4a-5a. By applying the *Mead* standards to an agency's interpretation of an ambiguous regulation, Petitioner respectfully submits that the Seventh Circuit has misread *Mead*, and in doing so, has abandoned *Auer*.[10]

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10. The Seventh Circuit's decision to formulate its own rule rather than apply the *Auer* standard to the IRS' interpretation of its ambiguous regulation underscores Justice Scalia's concern, articulated in his *Mead* dissent, that the *Mead* approach "will have a perverse effect on the rules that do emerge, given the principle (which the Court leaves untouched today) that judges must defer to reasonable agency interpretations of their own regulations." *Mead*, 121 S. Ct. at 2181.

The Seventh Circuit's clear failure to distinguish between the deference given to an agency's interpretation of an ambiguous statute, as opposed to an ambiguous regulation, significantly disrupts the administrative process and conflicts with the decisions of this Court and the decisions of other circuit courts.

### B. In Failing To Defer To The IRS' Interpretation Of Its Ambiguous Regulation, The Seventh Circuit's Decision Directly Conflicts With Decisions Of This Court.

Under the law set by this Court, it is well-settled that an agency's interpretation of an ambiguous *regulation* is subject to a very different set of standards of judicial deference than an agency's interpretation of an ambiguous *statute*. *Mead*, 121 S. Ct. at 2181; *Christensen v. Harris County*, 529 U.S. 576, 588, 120 S. Ct. 1655 (2000). By refusing to apply the regulatory standards to the IRS' interpretation of the partial termination regulation, the Seventh Circuit's decision in its Second Opinion directly conflicts with decisions of this Court. Most recently, in *Auer*, this Court held that an agency's interpretation of its own regulation, even if that interpretation is set forth in an informal document such as an *amicus curiae* brief or agency manual, is entitled to substantial deference when the regulation is ambiguous as to the question at issue. *Auer*, 519 U.S. at 461, 117 S. Ct. 905.

This is consistent with this Court's long held recognition of an agency's power and authority to interpret its own ambiguous regulations. *See, Thomas Jefferson University v. Shalala*, 512 U.S. 504, 512, 114 S. Ct. 2381 (1994) (agency's reasonable, consistently-held interpretation of its own regulation is entitled to deference); *Immigration and Naturalization Service v. National Center for Immigrants' Rights, Inc.*, 502 U.S. 183,

189-90, 112 S. Ct. 551 (1991) (same); *Stinson v. United States*, 508 U.S. 36, 44, 113 S. Ct. 1913 (1993) (if an agency's interpretation of its own regulation does not violate the Constitution or a federal statute, then it must be given controlling weight unless it is plainly erroneous).

In order to guarantee that the "rules will be written by 'masters of the subject' . . . who will be responsible for putting the rules into effect," *United States v. Moore*, 95 U.S. 760, 763, 24 L. Ed. 588 (1887), this Court grants "substantial judicial deference" to the IRS' reasonable, longstanding interpretation of its own regulations. *United States v. Cleveland Indians Baseball Co.*, 121 S. Ct. 1433, 1444 (2001). Indeed, as stated by this Court, the IRS' considered view on the interpretation of its regulations is generally entitled to considerable deference. *Jewett v. Com'r*, 455 U.S. 305, 318, 102 S. Ct. 1082 (1982). The rationale for the deference given to an agency's interpretation of its own ambiguous regulation is that the agency, and not the court, is in the best position to know what was intended by a regulation the agency drafts, implements and enforces. *Thomas Jefferson University*, 512 U.S. at 512-13, 114 S. Ct. 2381.

The Seventh Circuit's decision in the Second Opinion gives absolutely no deference or consideration to the IRS' interpretation of the ambiguous partial termination regulation or the IRS' expertise in the area of qualified employee benefit plans. This complete lack of deference is in direct conflict to this Court's well-established rule that an agency's reasonable and consistently held interpretation of its own ambiguous regulation is controlling and should be given substantial deference. *Auer*, 519 U.S. at 461, 117 S. Ct. 905. Petitioner respectfully submits that the Petition should be granted because the Second Opinion decides a federal question in a manner that is in direct conflict with this Court's opinions in *Cleveland*

*Indians Baseball Co.*, *Auer*, *Thomas Jefferson University*, *National Center for Immigrants' Rights, Inc.*, *Stinson* and *Jewett*.

### C. The Seventh Circuit's Lack Of Deference To The IRS' Interpretation Of The Regulation At Issue Directly Conflicts With The Decisions Of Other Circuit Courts.

Other circuit courts have recognized the validity of *Auer* and its controlling weight. The Seventh Circuit's failure, in its Second Opinion, to give deference to the IRS' reasonable, consistently-held interpretation of its ambiguous partial termination regulation is directly at odds with the decisions of these courts.[11]

For example, in *American Express Co. v. United States*, 262 F.3d 1376 (Fed. Cir. 2001), a post-*Mead* case, the Federal Circuit was faced with the question of what deference, if any, should be given to the IRS' interpretation of its own Revenue Procedure when the relevant regulation was silent as to the question at issue. The taxpayer challenged the IRS' reading of the Revenue Procedure and argued that no deference was due under *Chevron*, *Mead* or *Skidmore*. The Federal Circuit disagreed and stated that "substantial deference is paid to an agency's interpretations reflected in informal rulings," and that because the IRS' "interpretation [at issue] is reasonable, it attracts substantial judicial deference. . . ." *Id.* at 1383-84. Thus, the Court deferred to the IRS' interpretation. *Id.* at 1384.

Similarly, in *Bigelow v. Dept. of Defense*, 217 F.3d 875 (D.C. Cir. 2000), the District of Columbia Circuit was faced

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11. Because a number of circuit courts have issued decisions upholding *Auer* and its predecessors in numerous cases, Petitioner merely submits a sampling of those cases here and does not intend to identify each and every case where a circuit court recognized and followed *Auer*.

with the question of what deference, if any, should be given to an agency's interpretation of an ambiguous regulation which is advanced in the agency's litigation brief. The *Bigelow* Court held that despite the fact that the agency's position was advanced only in a legal brief, it was still entitled to deference under *Auer* because there was no reason to suspect the interpretation did not reflect the agency's fair and considered judgment. Specifically, the Court stated that "we have no reason to suppose that the interpretation of the regulations set forth in the [brief] is anything other than [the agency's] position. And we have been pointed to no past practices or pronouncements that are inconsistent with the [agency's] current interpretation." *Id.* at 878. Thus, the Court upheld the agency's interpretation, even though it was first advanced in litigation.

The Second Circuit has also addressed the issue of when deference is due an agency's interpretation of its own regulation. In *Esden v. Bank of Boston*, 229 F.3d 154 (2d. Cir. 2000), vested retirement plan participants filed a class action against the plan administrator under ERISA contending that the administrator had miscalculated the benefits due the participants who elected to receive a lump-sum distribution. The IRS, in an IRS Notice, had issued its interpretation of how the existing regulatory scheme regarding lump-sum distributions applied to the type of plan at issue. *Id.* at 169. Addressing a challenge to the IRS' regulatory interpretation, the Second Circuit stated that it is "well-settled that an agency's consistently held interpretation of its own regulation is entitled to deference" and that the interpretation "must be given controlling weight unless it is plainly erroneous or inconsistent with the regulation." *Id* at 168. Because the *Esden* Court found the IRS' interpretation both reasonable and consistently held, it found that the interpretation was entitled to deference under *Auer* regardless of its form or manner of publication. *Id.* at 169.

In addressing the issue, the Fourth Circuit stated that under *Auer*, an agency's regulatory interpretation proffered in the form of an *amicus curiae* brief is entitled to deference as long as there is no reason to suspect it is a post hoc rationalization to defend past agency action against attack. *Jones v. American Postal Workers Union National*, 192 F.3d 417, 427 (4th Cir. 1999). Likewise, in *Takacs v. Hahn Automotive Corp.*, 246 F.3d 776, 782 (6th Cir. 2001), the Sixth Circuit expressly recognizes that under *Auer*, where the regulation at issue is ambiguous, the agency's regulatory interpretation is controlling unless plainly erroneous or inconsistent with the regulation.

Both the Ninth and Eleventh Circuits have addressed the issue of regulatory deference where — like here — neither the statute nor the regulation answered or provided guidance on the issue in question. In both cases, the Circuit Courts deferred to the agency's informal interpretation. In *Foothill Presbyterian Hospital v. Shalala*, 152 F.3d 1132, 1133 (9th Cir. 1999), the plaintiff made a request for reimbursement under the Medicare statute. When the request was denied as untimely, the plaintiff sued the Secretary of Health in an attempt to obtain reimbursement. Neither the Medicare statute nor the controlling regulation answered the question of whether the plaintiff's request was timely. *Id.* at 1134-35. The Secretary of Health had informally interpreted the regulation in such a manner that would deny plaintiff its reimbursement request. Upon the plaintiff's challenge to the interpretation, the Ninth Circuit stated that if the regulation is silent or ambiguous "we will defer to the agency's interpretation unless an alternative reading is compelled by the plain language of the regulation." *Id.* at 1134. The Ninth Circuit then analyzed the Secretary's interpretation in light of the regulatory language and found the interpretation to be both reasonable and consistent with the regulatory language and scheme. *Id.*

Likewise, in *Falken v. Glynn County, Georgia*, 197 F.3d 1341 (11th Cir. 1999), both the relevant statute and regulation were silent on the question at issue. In *Falken*, dual function firefighters/emergency medical services (EMS) workers brought suit against the county seeking overtime under the Fair Labor Standards Act ("FLSA"). The county responded that it was entitled to the FLSA's partial overtime exemption for employees engaged in fire protection activities. *Id.* at 1344. The FLSA does not define "fire protection activities." Although the Department of Labor ("DOL"), the agency charged with implementing the FLSA, had issued notice and comment regulations defining "fire protection activities," the regulations did not answer the precise question at issue in *Falken*. *Id.* at 1345-47.

The DOL, however, had issued an opinion letter setting forth certain criteria to be used to determine if dual function firefighters/EMS workers fit within the regulatory definition of "fire protection activities." *Id.* at 1349. Citing *Auer*, the Eleventh Circuit stated that "we must defer to the DOL's interpretation of its FLSA regulations unless the interpretation is 'plainly erroneous or inconsistent with the regulation.'" *Id.* at 1350. Because the Court found that the DOL's interpretation was a permissible interpretation of the regulation and the FLSA, the statute at issue, it held that the criteria set forth in the DOL opinion letter governed the fire protection activities exemption to dual function firefighters/EMS workers. *Id.* The Court then remanded the case to the district court for further proceedings regarding the application of the DOL criteria. *Id.* at 1353.

Cardinally, both the Ninth and the Eleventh Circuits have found *Auer* applicable even in circumstances where both the relevant statute and regulation are silent or ambiguous as to the issue in question. *Foothill Presbyterian Hospital*, 152 F.3d at 134-35; *Falken*, 197 F.3d at 1345-47. Indeed, since a court will look to regulations and regulatory interpretations *only* when the

relevant statute is silent or ambiguous, *Auer* would be moot if it were to apply only when the regulation, but not the statute, is ambiguous or silent. Clearly, since *Mead* did not overrule *Auer* in any respect, this cannot be the case, and *Auer* should continue to apply post-*Mead*.

The Seventh Circuit's apparent refusal to apply *Auer* after *Mead* to an agency's interpretation of its own ambiguous regulation directly contradicts the circuit court cases cited, *supra*, particularly the Ninth Circuit's decision in *Foothill Presbyterian Hospital* and the Eleventh Circuit's decision in *Falken*. On this issue, the Seventh Circuit appears to stand alone. Petitioner respectfully submits that this Petition should be granted in order to clarify the law as to the proper deference to be given to an agency's interpretation of its own ambiguous regulation and to bring uniformity to the circuit courts on this matter.

## III. THE SEVENTH CIRCUIT INCORRECTLY DECIDED AN IMPORTANT QUESTION INVOLVING THE INTERPLAY BETWEEN STANDARDS OF JUDICIAL DEFERENCE UNDER *MEAD* AND THOSE UNDER *AUER*, WHICH QUESTION HAS NOT BEEN, BUT SHOULD BE, SETTLED BY THIS COURT.

This case involves the important and recurring interplay between an agency's informal interpretation of a statute and an agency's informal interpretation of its own regulation. Federal agencies are involved in virtually all aspects of Americans' business and financial life, and are constantly issuing rulings, interpretations, opinions and regulations. Thus, the interplay between an agency's informal interpretation of statutes and regulations is of obvious and constant importance to courts, litigants and agencies. This Court has not yet addressed the subject of what type of deference is appropriate when an agency

has issued informal interpretations of both an ambiguous statute *and* an ambiguous regulation. Petitioner submits that litigants, courts and federal agencies need the prompt assistance of this Court to answer the important questions of judicial deference presented here.

An agency's informal interpretation of an ambiguous statute is given substantial judicial deference under *Chevron* if that interpretation meets the standard articulated in *Mead*: administrative implementation of a statute qualifies for *Chevron* deference when it appears that Congress delegated authority to the agency generally to make rules carrying the force of law and that the agency interpretation claiming deference was promulgated in an exercise of that authority. *Mead*, 121 S. Ct. at 2171. Absent *Chevron* deference, an agency's interpretation of a statute it administers is entitled to respect commensurate with its degree of persuasiveness. *Mead*, 121 S. Ct. at 2175. The *Mead* Court affirmed the *Skidmore* Court's recognition that there are degrees of deference to be accorded an agency interpretation depending on the persuasiveness of the agency's position. *Mead*, 121 S. Ct. at 2172; *Skidmore*, 323 U.S. at 140, 65 S. Ct. 161. Thus, under *Skidmore*, the amount of deference given depends entirely on whether a court is "persuaded" by the agency's interpretation. As this Court is undoubtedly aware, an agency's power of persuasion, and a court's willingness to be persuaded, are widely divergent. In all likelihood, there will be substantial differences among circuits regarding the deference given to various agency interpretations of ambiguous statutes.

On the other hand, an agency's informal interpretation of its own ambiguous regulation is given much greater deference than that afforded under *Mead* and *Skidmore*. Specifically, an agency's informal interpretation of an ambiguous regulation — regardless of the interpretation's form (*i.e.*, agency manual, *amicus curiae* brief, etc.) — is given controlling weight and

should be deferred to unless plainly erroneous or inconsistent with the regulation at issue. *Auer*, 519 U.S. at 461, 117 S. Ct. 905. Thus, under *Auer*, an agency's interpretation of its own regulation will generally be upheld, and a litigant would have a much more difficult time advancing his or her own regulatory interpretation. Because the agency is interpreting a regulation it promulgated after considered review and analysis of how best to implement the statute upon which the regulation is based, there will *not*, in all likelihood, be substantial differences among circuits regarding the deference given to an agency's interpretation of its own ambiguous regulation.

The question then becomes what standards apply when the agency has issued an informal interpretation of *both* an ambiguous statute *and* an ambiguous regulation. Since a court will only look to statutory and regulatory interpretations when the relevant statute is silent or ambiguous, *Auer* must be applicable in circumstances where both the relevant statute and relevant regulation are silent or ambiguous as to the issue in question. In such instances, the agency often issues an interpretation which can fairly be called a statutory *and* regulatory interpretation. Clearly, *Chevron, Mead, Skidmore* and *Auer* must be read together in a coherent manner so as not to render *Auer* moot, particularly where — as here — the controlling regulation gives the agency the express authority to interpret the regulation.

In order to do so, Petitioner submits that (i) *Chevron,* (ii) *Mead* and *Skidmore* and (iii) *Auer* should be applied in a three step process. First, if the statute is ambiguous and the agency has issued an interpretation of the statute, then it should be determined whether the interpretation is formal or otherwise carries the "force of law." If so, then the interpretation should be given *Chevron* deference. Second, if the statutory interpretation is not deserving of *Chevron* deference, then it

should be determined whether the interpretation should be given *Skidmore* deference. If *Skidmore* deference is given, then the analysis should stop there. However, if *Skidmore* deference is not given and the agency has issued an interpretation of its ambiguous or silent regulation, then the court must take the third step and apply *Auer*, which step the Seventh Circuit failed to take here.

The adoption of this three-step process, or any other clarification by this Court of the interrelationship between an agency's statutory and regulatory interpretations, would ensure that the federal courts are consistent in their treatment of an agency's statutory and regulatory interpretations and that agency interpretations are accorded substantially the same amount of deference by the courts. Correspondingly, litigation surrounding an agency's interpretation of a statute and a regulation would be greatly reduced.

On the other hand, if this Court does not clarify this issue, several problems result. First and foremost, the lack of clarification would allow future litigants to challenge virtually every formal or informal agency interpretation of its own regulation by asserting that the *litigant's* reading of the regulation is more reasonable than the agency's and should control. Every agency decision would be required to be reviewed on a post hoc basis. Clearly, this is not consistent with *Auer* or *Mead*, where, in his dissent, Justice Scalia's stressed that "judges must defer to reasonable agency interpretations of their own regulations." *Mead*, 121 S. Ct. at 2181. Notably, the majority did not disagree with Justice Scalia on this point.

Second, federal agencies would be faced with widely divergent opinions regarding the deference given to their statutory and regulatory interpretations. Thus — as in this case here — in one jurisdiction, the agency's interpretation is followed, and in another jurisdiction, a different interpretation

of the regulation could be followed. Multiple rules could develop. Finally, refusing to apply *Auer* to an agency's interpretation of a regulation where the agency has also issued a statutory interpretation will encourage a litigant to "forum shop" for the interpretation the litigant seeks depending on the type of deference the litigant desires. By combining *Chevron*, *Mead*, *Skidmore* and *Auer* into one process, these problems are eliminated.

In failing to recognize or address the interplay between an agency's statutory and regulatory interpretations, the Seventh Circuit erred on an important issue of law. Petitioner respectfully submits that this Petition should be granted in order for this Court to answer the important questions of judicial deference presented here.

## CONCLUSION

For the foregoing reasons, Petitioner respectfully requests that this Court grant the Petition for a Writ of Certiorari.

Respectfully submitted,

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